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C O N F I D E N T I A L SECTION 01 OF 03 HARARE 001664

SIPDIS

NSC FOR SENIOR AFRICA DIRECTOR JENDAYI FRAZER
LONDON FOR CGURNEY
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TAGS: ECON PGOV ETRD ZI
SUBJECT: ZIMBABWE FINANCE MINISTER PROVIDES STARK ECONOMIC PICTURE IN LETTER TO CABINET

Classified By: political section chief Matt Harrington.
Reasons: 1.5 (B) and (D).

Summary

¶1. (C) In a June 25 letter to the Cabinet's economic and finance committe, Finance Minister Simba Makoni provided a stark picture of Zimbabwe's economic crisis. According to Makoni, Zimbabwe has no foreign exchange reserves, which has prevented the Government from procuring even those products it has identified as most critical -- drugs, fuel, electricity, and grain -- and paying even its most understanding creditors (Zimbabwe's external arrears now total U.S. $1.36 billion.) HCB Mozambique has recently reduced electricity supplies due to non-payment and ESKOM South Africa has designated Zimbabwe an "interruptible" customer. Payments are also long overdue to fuel suppliers; more than a third of the GOZ's U.S. $106 million debt in the fuel sector is owed to the Libyan Arab Foreign Bank, but funds are not available to meet that commitment. The GOZ can no longer afford to buy sufficient quanitities of chemicals for treatment of drinking water, posing a major public health hazard, and it is unable to cover the costs of its diplomatic missions overseas. A major shortfall -- estimated to be U.S. $1.15 billion -- in forex requirements between now and March 2003 will result in either critical shortages of essential inputs or further build up in external arrears. The fact that we have a copy of Makoni's letter should be strictly protected, as it was an internal document not intended for circulation outside of Cabinet. End Summary.

General economic indicators

¶2. (C) On July 17, a reliable embassy contact with excellent sources in the Zimbabwean government provided us with a copy of a private June 25 letter from Finance Minister Simba Makoni to the Cabinet committee on financial and economic affairs. The letter provides a stark assessment of the country's economic crisis, and describes in some detail the GOZ's spending priorities, arrearages to key creditors, and financial arrangements with Libya. We have summarized key excerpts in this cable and have forwarded the letter by classified pouch to AF/S.

Begin Excerpts from Minister Makoni's letter:

¶3. (C) Zimbabwe "has no usable foreign exchange reserves," which has adversely affected the country's ability to procure critical imports such as drugs, fuel, electricity, raw materials, and grain. In addition, Zimbabwe has failed to meet its foreign payment obligations "resulting in the suspension of disbursements of critical project-related loans, thus worsening the balance of payments position." As of mid-June, Zimbabwe's total external payment arrears were U.S. $1.36 billion.

¶4. (C) A GOZ External Payments Committee (EPC) earlier decided to allocate scarce resources to certain critical sectors of the economy, but the GOZ does not have even sufficient funds for these top priority areas:

--grain, fuel, electricity, drugs, and currency swaps;
--creditors likely to disburse funds quickly, such as the Kuwait Fund and Badea;
--multilateral institutions;
--overseas embassies and critical CPO payments (PFMS and Security);
--water treatment chemicals

Electricity debts

¶5. (C) The Zimbabwe Electricity Supply Authority (ZESA) owes its electricity suppliers U.S. $21 million and spare parts suppliers U.S. $7.4 million. ZESA's monthly foreign currency requirements average U.S. $12 million, but the GOZ has only

been able to allocate a monthly average of U.S. $5.3 million since January, leaving a significant shortfall. ZESA's principal creditors in this sector are
ESKOM (S. Africa), owed U.S. $5.07 million since 6/14/02; HCB (Mozambique), owed U.S. $6.67 million since 4/30/02; EDM (Mozambique), owed U.S. $4.14 million for wheeling charges since 4/30/02; SNEL (DRC), owed U.S. $4.15 million since 2000; and ZESCO (Zambia), owed U.S. $1.09 million since 2000.

¶6. (C) HCB Mozambique has decided to reduce electricity supplies to ZESA effective 6/30/02 due to non-payment, while ESKOM has made ZESA an "interruptible" customer, meaning its supplies can be reduced at any time. Meanwhile, SNEL DRC has, since April 2002, demanded payment in hard currency.

Fuel debts

¶7. (C) The National Oil Company of Zimbabwe (NOCZIM) is in arrears to the tune of U.S. $106 million, and payments are long overdue. NOCZIM's largest creditor, by far, is the Libyan Arab Foreign Bank, which was owed U.S. $43 million as of June 22, but funds are not available to meet this commitment. Other major creditors are BP South Africa (owed U.S. $17.8 million since 1999); IPG (owed U.S. $17.8 million since 2000); Engen South Africa (owed U.S. $12 million since 1999); Caltex (owed U.S. $7.8 million since 1999); the Government of Botswana (owed U.S. $4.4 million since 2000); and Mobil Africa (owed U.S. $1.1 million since 1999).

¶8. (C) The GOZ's agreement with the Libyan Area Foreign Bank provides for NOCZIM to deposit the Zimbabwe dollar equivalent of oil supplied in an account at the Commercial Bank of Zimbabwe (CBZ). The funds in that account are then used by the Libyan authorities to make investments in Zimbabwe. The only investments made so far, however, have been the purchase of Commercial Bank of Zimbabwe shares worth U.S. $6.7 million. When Zimbabwe was unable to settle its debt of U.S. $43 million on June 22, Tamoil suspended all deliveries of petroleum products to NOCZIM. (Note: we do not know whether this debt has subsequently been paid. End note.) Until that amount is paid, "it would be difficult for NOCZIM to negotiate for the renewal of the U.S. $90 million Financing Facility through the Libyan Arab Foreign Bank." (Note: A separate contact informed us that the GOZ delegation that traveled to Tripoli in late June to renegotiate the facility encountered a frosty reception. End note.)

Air Zimbabwe/Eximbank

¶9. (C) Makoni notes the agreement reached in May among his Ministry, the Ministry of Transport and Communication, and Air Zimbabwe to repay Eximbank for the airline's two Boeing 767's -- U.S. $5 million each in April and May, U.S. $6 million each in June, July, and August, and a final U.S. $4.6 million payment in September. Makoni warns that the aircraft will be impounded in the event of non-payment, and reports that, in apparent anticipation of such action, "creditors" have written to the GOZ advising of their intention to send inspectors to examine the aircraft.

Zimbabwe's embassies

¶10. (C) The GOZ continues to have serious difficulties in covering the costs of its overseas diplomatic missions. A U.S.$2 million payment was made in May to cover a portion of costs incurred in January, while an additional U.S. $2.1 million was disbursed in June to cover a portion of January and February costs. Makoni stresses that "the situation at embassies is now very critical and there is urgent need to pay another U.S. $4 million."

Medicines/Health

¶11. (C) The GOZ has been unable to fulfill its committment to allocate U.S. $2 million every month to import drugs and health equipment, due to the forex shortage. A total of only U.S. $3.5 million has been allocated for this purpose since January. The shortage of medicines and health equipment has, according to Makoni, "crippled the health delivery system."

Cashflow

¶12. (C) Zimbabwe's foreign exchange requirements between April 2002 and March 2003, according to Makoni, will amount to U.S. $1.15 billion, but the supply is expected to be only U.S. $486.4 million. The consequent shortfall of $660 million will result in critical shortages of essential inputs or further build up in external payment arrears.

External Payment Arrears -- IFI's and other key donors

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¶13. (C) Zimbabwe continues to accumulate arrears to multilateral financial institutions. As of mid-June, arrears to the IMF total U.S. $131.3 million; to the World Bank, U.S. $130.9 million; and to the ADB, U.S. $146.3 million. In addition, there are outstanding payments to creditors "likely to disburse," such as Badea
(U.S. $1.5 million for telecommunications), the Kuwait Fund (U.S. $500,000 for road improvements); China (U.S. $2.6 million for defense); and IFAD (U.S. $2.2 million for agricultural assistance).

Impact on the Economy

¶14. (C) Makoni concludes by emphasizing that the unavailability of forex has worsened shortages of raw materials, machinery and equipment, and chemicals. Consequently, production in the key sectors -- agriculture, manufacturing, mining, and tourism -- is severely constrained, undermining the capacity of the economy to generate foreign exchange. This cycle could be exacerbated if fuel and electricity supplies are reduced due to non-clearance of arrears. The forex shortage will increase the difficulty of obtaining fertilizers and other agricultural inputs, casting doubt on the success of the resettlement program. It will also further constrain service delivery in the health sector; shortages of chemicals for treating water, for instance, are "already posing a major health hazard."

End Excerpts from Makoni letter.

Comment

¶15. (C) Makoni has provided a sobering picture of the devastation wrought by the Mugabe regime's harebrained economic mismanagement. The letter confirms that the Finance Minister is as frank in private with his ruling party colleagues as he is in public. It also confirms that GOZ decision-makers are well aware of the deleterious impact of their policies. Growing realization of the potentially catastrophic consequences of the forex shortage could explain recent moves by the Reserve Bank to crack down on bureaux de change and other legitimate institutions who deal in the parallel currency market. Further aggressive GOZ regulatory efforts, however, could force parallel rate cash flows to such legitimate institutions into the black market.

¶16. (C) Please strictly protect the fact that we have a copy of Makoni's letter, as it was not intended for circulation outside of Cabinet. In addition, the well-respected Makoni is reportedly considered by some of his more moderate ruling party colleagues as a successor to Mugabe, but publication of the letter's contents could be used against him by other -- less palatable -- pretenders to the throne.

SULLIVAN